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No. 97-607

# In the Supreme Court of the United States

OCTOBER TERM, 1997

JOHN R. MCCARRON, PETITIONER

*v.*

FEDERAL DEPOSIT INSURANCE CORPORATION, AS RECEIVER OF MERITOR SAVINGS BANK AND IN ITS OWN CAPACITY

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT*

## BRIEF FOR THE RESPONDENT IN OPPOSITION

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## QUESTIONS PRESENTED

1. Whether benefits payable to a former executive of a failed insured depository institution under a severance agreement are "actual direct compensatory damages" for which the Federal Deposit Insurance Corporation (FDIC), as receiver, is liable under 12 U.S.C. 1821(e)(3), even though the FDIC has lawfully repudiated the agreement.

2. Whether the court of appeals erred in ruling that petitioner had not met the requirements to qualify for an exception to a proposed FDIC regulation that would have prohibited his severance agreement.

3. Whether the court of appeals erred in deciding that the FDIC had not abused its discretion, as receiver, to repudiate petitioner's severance agreement because the receivership had surplus funds four years after the repudiation.

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### OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-19a) is reported at 111 F.3d 1089. The opinion of the district court (Pet. App. 20a-26a) is unreported.

### JURISDICTION

The judgment of the court of appeals was entered on May 1, 1997. A petition for rehearing was denied on July 8, 1997. Pet. App. 35a-36a. The petition for a writ of certiorari was filed on October 6, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## STATEMENT

1. The Federal Deposit Insurance Corporation (FDIC), as receiver for a failed insured depository institution, is authorized to repudiate any contract to which the institution is a party the performance of which the FDIC, in its discretion, determines will be burdensome and the repudiation of which the FDIC, in its discretion, determines will promote the orderly administration of the institution's affairs. 12 U.S.C. 1821(e)(1). The liability of the FDIC for any repudiation is "limited to actual direct compensatory damages." 12 U.S.C. 1821(e)(3)(A). "[D]amages for lost profits or opportunity" are expressly excluded. 12 U.S.C. 1821(e)(3)(B)(ii). A claimant whose claim has been disallowed by the FDIC may file suit either in the district court for the district within which the depository institution's principal place of business is located or in the United States District Court for the District of Columbia. 12 U.S.C. 1821(d)(6)(A).

2. On December 11, 1992, the Secretary of Banking for the Commonwealth of Pennsylvania declared Meritor Savings Bank (Meritor) insolvent and appointed the FDIC receiver. Pet. App. 3a. In its capacity as receiver, the FDIC executed a Purchase and Assumption Agreement transferring a portion of Meritor's assets and liabilities to Mellon Bank (Mellon). *Ibid.* The FDIC retained the liabilities not assumed by Mellon and the assets not purchased by Mellon, which the FDIC proceeded to liquidate for the benefit of Meritor's approved creditors. *Ibid.*

Prior to its insolvency, in 1988, Meritor had hired petitioner as its Executive Vice President and General Counsel. Pet. App. 2a. Meritor had agreed to pay petitioner severance benefits under either of two

mutually exclusive agreements. *Ibid.* A Severance Compensation Agreement (SCA) provided that petitioner would receive a lump sum equal to twice his annual salary, as well as the continuation of certain insurance benefits for 24 months, if Meritor discharged him without cause. *Id.* at 2a-3a. Under a separate Agreement for Compensation on Discharge Subsequent to a Change in Control (CIC), if Meritor discharged him without cause in a "change in control," the bank agreed to pay petitioner three times his annual salary and to extend insurance benefits for 36 months. *Id.* at 2a. Petitioner was also covered under Meritor's Separation Pay Plan (SPP), an employee benefit plan that covered all Meritor employees and provided severance pay under certain circumstances based upon years of service with the bank. *Id.* at 3a. Meritor also provided petitioner with benefits under its Supplementary Unfunded Retirement Plan (SURP), a non-qualified pension plan for highly paid executives designed to supplement the retirement payments available to them under Meritor's qualified plan. *Ibid.* On the day that the Secretary of Banking closed Meritor, the FDIC informed petitioner and other Meritor employees that the FDIC would not make severance payments to the employees. *Ibid.*

3. In March 1994, petitioner filed suit in federal district court, seeking severance and retirement benefits. Pet. App. 4a-5a. On January 26, 1996, the district court entered judgment for the FDIC based upon the Third Circuit's decision in *Hennessy* v. *FDIC*, 58 F.3d 908 (1995), cert. dismissed, 116 S. Ct. 688 (1995), cert. denied, 116 S. Ct. 1318 (1996), in which the court of appeals held that the FDIC had lawfully repudiated Meritor's severance obligations under the SPP to both its executives and its other employees.

Pet. App. 20a-26a. The *Hennessy* court held, further, that the former employees were not entitled to severance benefits as "actual direct compensatory damages" arising from the repudiation. See 58 F.3d at 918-921. The district court determined that *Hennessy* controlled petitioner's severance claims under his individual severance agreements as well as under the SPP. Pet. App. 22a-24a. The district court also held that petitioner was not entitled to retirement benefits under the SURP because his benefits had not vested at the time of the FDIC receivership. *Id.* at 24a-25a.

4. The court of appeals affirmed the district court's judgment on petitioner's severance claims but remanded for further consideration of petitioner's claim for retirement benefits under the SURP. Pet. App. 1a-19a. The court of appeals held that petitioner had no claim for benefits under the CIC because "the triggering events contemplated by it never occurred." *Id.* at 11a-12a. The court of appeals characterized petitioner's SCA as a standard severance agreement, "virtually indistinguishable" from the SPP at issue in *Hennessy*, and held that the FDIC's repudiation of Meritor's severance obligations also encompassed that agreement. *Id.* at 8a-10a. Applying its holding in *Hennessy* that claims for severance benefits are analogous to liquidated damages and are not "actual direct compensatory damages" for which Section 1821(e)(3) allows recovery, the court found that the FDIC was not liable for repudiation damages. *Id.* at 10a-11a.

The court of appeals also rejected petitioner's argument that he was nonetheless entitled to benefits under an FDIC regulation promulgated in 1996, six years after petitioner entered into his severance

agreements with Meritor. The regulation, 12 C.F.R. Pt. 359, bans certain employee-specific severance agreements called "golden parachutes" but provides an exception to permit troubled institutions to enter into those agreements with individuals, known as "white knights," who are hired to help restore an institution to profitability. The court determined that the regulation could not support petitioner's severance claim, even assuming petitioner was a white knight, because the exception to the ban on golden parachutes is not applicable unless the institution's "appropriate federal banking agency and the FDIC 'consent in writing to the amount and terms of the golden parachute payment.'" Pet. App. 14a (quoting 12 C.F.R. 359.4). The court thus concluded that there was "no factual or legal basis to permit payment of [petitioner's] severance claims under the FDIC rules governing the white knight exception." *Ibid.* The court of appeals noted, further, that the FDIC regulation specifically provides that the receiver for a failed bank would not be obligated to pay the promised golden parachute, even if the payment was pre-approved. *Id.* at 14a-15a. Finally, the court of appeals rejected petitioner's challenge to the lawfulness of the FDIC's repudiation based on the current solvency of the Meritor receivership. The court explained that petitioner had not presented any facts indicating why and how the receivership became solvent and refused to "us[e] 20/20 hindsight" to evaluate the FDIC's initial determination that honoring the severance agreements would have been burdensome. *Id.* at 19a n.4.

## ARGUMENT

The Third Circuit correctly held that the FDIC is not liable to petitioner for severance payments as damages for its lawful repudiation of the severance agreement between petitioner and Meritor. Although other courts of appeals have allowed former bank employees to recover severance benefits from the FDIC, the narrow issue of the FDIC's liability for severance benefits as repudiation damages does not present a conflict that is likely to have broad future impact. The other issues pressed by petitioner are fact-bound and do not implicate any important question of federal law. Accordingly, further review by this Court is not warranted.

1. a. The court of appeals correctly interpreted 12 U.S.C. 1821(e) to permit the FDIC to repudiate a severance agreement without becoming liable for the severance payments that it has repudiated as "actual direct compensatory damages" for the repudiation. Congress intended through Section 1821(e)(3) "to pare back damage claims founded on repudiated contracts." See *Howell* v. *FDIC*, 986 F.2d 569, 572 (1st Cir. 1993). Congress therefore expressly provided that the FDIC would not be liable for the full range of damages for which a party who repudiates a contract would ordinarily be liable. *Id.* at 573. Thus, Congress limited liability to "actual direct compensatory damages" and expressly excluded from that term "damages for lost profits and opportunity," as well "punitive or exemplary damages" and "damages for pain and suffering." See 12 U.S.C. 1821(e)(3).

Severance payments are an estimate, made at the time of employment, of potential losses as a result of the termination of employment. They thus fall

squarely within the "damages for lost * * * opportunity" for which Congress explicitly barred FDIC liability. Moreover, because they are stipulated in advance, severance payments are unlikely, except by happenstance, to compensate for "actual direct" losses suffered by a terminated employee. Indeed, in petitioner's case, the severance payments under the SCA would have been twice his annual salary and would have been in addition to payments made to petitioner as an ordinary employee under the SPP. As the First and Third Circuits have recognized, severance payments are designed to be an easily determined proxy for possible loss from foregone alternative employment and to avoid problems of proof and disputes over an employee's ability to mitigate damages by finding new employment. See *Howell*, 986 F.2d at 573; *Hennessy* v. *FDIC*, 58 F.3d 908, 921 (3d Cir. 1995), cert. dismissed, 116 S. Ct. 688 (1995), cert. denied, 116 S. Ct. 1318 (1996). Severance payments are therefore more akin to "liquidated damages" than they are to the "actual direct compensatory damages" permitted by the statute. See *Howell*, 986 F.2d at 573 (citing E. Allan Farnsworth, *Contracts* § 12.18 (2d ed. 1990), and Charles McCormick, *Damages* § 146 (1935)). See also *Hennessy*, 58 F.3d at 921.

The specific rules governing the availability of damages for repudiation of leases in Section 1821(e)(4) confirm a reading of the general provisions that bars compensation for estimates of lost employment opportunity. If the FDIC repudiates a lease, it is liable for rent until the time of the repudiation but not for future rent. See 12 U.S.C. 1821(e)(4)(B). "As with severance pay, the lessor may have foregone other opportunities but the loss is not to be recompensed." *Howell*, 986 F.2d at 573.

The plain language of Section 1821(e)(3) and of related statutory provisions thus confirms the conclusion of the court of appeals. Indeed, the contrary conclusion would give the damage provision of Section 1821(e)(3) the practical effect of denying the FDIC the right to repudiate severance agreements that is clearly granted by Section 1821(e)(1). Under that reading of the statute, the FDIC would always owe damages equal to the payments that it would have owed if it had instead affirmed the agreements.

b. Petitioner argues, however, that this Court should grant certiorari to resolve a conflict among the courts of appeals, which are divided on the issue whether the FDIC is liable for damages when it lawfully repudiates a severance agreement. The Third Circuit, in this case and in *Hennessy*, *supra*, as well as the First Circuit in *Howell*, *supra*, have held that severance payments do not constitute "actual direct" damages because the payment amounts are estimates of potential damages from lost employment opportunity, akin to liquidated damages. The District of Columbia, Ninth, and Eleventh Circuits have disagreed and have held that severance payments are "actual direct compensatory damages" within the meaning of Section 1821(e)(3). See *Office & Professional Employees Int'l Union, Local 2* v. *FDIC*, 27 F.3d 598 (D.C. Cir. 1994) (*OPEIU*); *Monrad* v. *FDIC*, 62 F.3d 1169 (9th Cir. 1995); *McMillian* v. *FDIC*, 81 F.3d 1041 (11th Cir. 1996). The disagreement among those courts of appeals is unlikely to be of broad future significance, however, and therefore does not require resolution by this Court at this time.

There are no longer any cases pending in the lower courts involving the question whether a receiver's

repudiation of a severance agreement gives rise to damages, and there are not likely to be a significant number of such cases in the future. In 1993, after the dispute in this case arose, Congress enacted a national depositor-preference statute, 12 U.S.C. 1821(d)(11), which requires that all insured and uninsured depositors be paid in full before any general creditor. Under the new preference rules, severance claims would arise only in those relatively few instances in which a receivership has assets remaining after all of the depositors' claims have been fully satisfied. In addition, there has been a dramatic reduction in the number of bank failures in recent years, in part as a result of a healthy economy, but also due to improvements in bank and thrift regulation implemented by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, and the Federal Deposit Insurance Corporation Improvement Act of 1991, Pub. L. No. 102-242, 105 Stat. 2236.*

If a dispute over the FDIC's liability for severance benefits should arise, it is likely that plaintiffs in the First and Third Circuits will take advantage of the choice of venue provided them by 12 U.S.C. 1821(d)(6)(A) to bring themselves under the rule of the District of Columbia Circuit in *OPIEU*. All plaintiffs

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* In 1996, the FDIC closed only six insured depository institutions. FDIC, *Annual Report—1996*, at 24, 25, 111. To date in 1997, there have been no bank failures. *The Condition of the Banking and Thrift Industries: Hearings Before the Subcomm. on Financial Institutions and Regulatory Relief of the Senate Comm. on Banking, Housing, and Urban Affairs*, 105th Cong., 1st Sess. 3 (Oct. 21, 1997) (testimony of Andrew C. Hove, Jr., Acting Chairman, FDIC); FDIC, *FDIC Quarterly Banking Profile* 3 (Second Quarter 1997).

thus have the ability as well as the incentive to pursue their claims in fora that adhere to the same reading of the statute. In any event, this Court would have the opportunity to revisit the meaning of Section 1821(e)(3) if a new dispute arose. Thus, resolving the disagreement among the courts of appeals would not be a worthwhile use of this Court's resources at this time.

2. Petitioner also argues (Pet. 7-10) that the Court should grant certiorari because the court of appeals rejected his claim that his severance agreements should have been honored under the white knight exception to the golden parachute regulation. The fact-bound claim that the court of appeals misapplied the regulation to the circumstances of petitioner's case does not warrant review. The court of appeals correctly concluded that petitioner is not covered by the exception. Petitioner does not dispute that the FDIC did not "consent in writing to the amount and terms" of his severance agreement and that written consent is an explicit condition precedent to the application of the exception. See 12 C.F.R. 359.4. In any event, the regulation is irrelevant to petitioner's case. The FDIC did not rest its denial of petitioner's severance claim on the regulation. Indeed, as petitioner admits, the regulation was not even in effect when petitioner and Meritor entered into the severance agreements. The court of appeals discussed the regulation in its opinion only because petitioner sought to avail himself of the exception.

Petitioner's contention (Pet. 7-10) that the decision of the court of appeals regarding the regulation conflicts with the holding in *United States* v. *Winstar Corp.*, 116 S. Ct. 2432 (1996), has no basis. In *Winstar*, this Court held the United States liable for breach of

contract when it declined to honor agreements permitting the use of certain accounting methods that were prohibited by a subsequent change in law. Petitioner maintains (Pet. 9) that the court of appeals contravened the holding in *Winstar* by allowing the FDIC "to revoke its prior approval of the [severance] agreement" based on a new regulation, without incurring any liability for damages. Contrary to petitioner's contention, the court of appeals did not hold that the FDIC revoked any prior approval of the terms and conditions of petitioner's agreement. Nor did the FDIC or the court of appeals rely on the new regulation as the basis for the denial of petitioner's severance benefits. As described above, the court of appeals ruled that petitioner could not avail himself of the exception to the regulation because the FDIC had never consented in writing to the terms of his severance agreement. Pet. App. 14a. The court's further observation that, even if petitioner had obtained prior written approval, the FDIC could have validly repudiated the contract is merely dictum that was unnecessary to its resolution of petitioner's claim. Thus, petitioner's argument lacks merit.

3. Finally, petitioner suggests (Pet. 11) that this Court should grant certiorari to review his assertion that he is "a general creditor who should be paid by the receiver before distribution to subordinated creditors and to shareholders." The court of appeals addressed that claim in a footnote, observing that the factual basis for petitioner's contention, raised in a letter submitted pursuant to Federal Rule of Appellate Procedure 28(j), merely established a surplus in the receivership as of October 1996. Pet. App. 19a n.4. Noting that petitioner had presented no facts "indicat[ing] when and how [the receivership] became

solvent," the court declined to "us[e] 20/20 hindsight" to evaluate the FDIC's determination in 1992 that affirmation of petitioner's severance agreement would have been burdensome. *Ibid.* The court of appeals' determination that petitioner did not present facts sufficient to support his claim that a surplus in the receivership in 1996 showed that the FDIC abused its discretion when it repudiated his severance agreement in 1992 presents no issue warranting review.

## CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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